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No. 87-1467

IN THE
Supreme Court of the United States
OCTOBER TERM, 1988

EXXON COMPANY, U.S.A.,
A DIVISION OF EXXON CORPORATION,
Petitioner,

v.

BANQUE DE PARIS ET DES PAYS-BAS,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

I. PARIBAS HAS CONCEDED THE CENTRAL ISSUES OF FEDERAL DIVERSITY PRACTICE RAISED BY THIS CASE

The question presented in this case is whether a federal court sitting in diversity—here, either the Fifth Circuit or this Court—should consider and follow a relevant post-judgment state decision that has been brought to the federal court's attention while the diversity case is *sub judice*. In opposing certiorari, Paribas argued only that

the state decision, *Kerr Construction Co. v. Plains National Bank*, No. 07-86-0205-CV (Tex. App. — Amarillo 1987, writ denied), could not properly be considered because it had not been ordered published. Br. in Opp. 3-5. Publication of that decision, however, has now been ordered (and the opinion is to be published at 753 S.W.2d 181). *See* Exxon Supp. Br. 1. As a consequence, Paribas no longer argues that this case should or even could be decided on the merits without reference to *Kerr Construction*.[1]

Major portions of this case therefore appear to have been resolved. Exxon's opening brief demonstrated that a court of appeals must reconsider its judgment in a diversity case in light of a new state decision brought to its attention prior to the expiration of time for filing a petition for certiorari. Exxon Br. 20-28. Exxon further showed that this Court, once it grants certiorari, has a duty to decide a diversity case in accordance with existing state law. *Id.* at 29-32. Paribas makes no argument to the contrary and thus concedes the central issues of federal diversity practice raised by this case.

Paribas in effect has entered a plea of confession and avoidance. Paribas implicitly acknowledges that *Kerr Construction* must be considered in deciding this case on the merits, but it argues that that decision should not be followed because (1) the Texas intermediate court of

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[1] Although Paribas formally acknowledges that the apparent complications introduced into the case by nonpublication of *Kerr Construction* have been removed, Paribas Br. 11-13, Paribas asserts, in a parting shot, that "it is clear" that diversity courts must follow state no-citation rules with respect to unpublished opinions. *Id.* at 12. That position, which already had been rejected by the First and Sixth Circuits, *see* Exxon Br. 37, has now been rejected by the Third Circuit as well. *Craig v. Lake Asbestos of Quebec, Ltd.*, 843 F.2d 145, 152 n.6 (3d Cir. 1988).

appeals misapplied Texas law, Paribas Br. 13-19, and (2) the Texas Supreme Court has confirmed that the decision was erroneous. *Id.* at 20-22. This Court ordinarily does not address such arguments. When matters of state law are presented, the Court's usual practice is either to remand the case to the court of appeals or to certify the issue to the state supreme court.

The arguments under Texas law and practice advanced by Paribas, however, have two important implications for federal diversity practice. The first concerns the deference owing to a decision of a state intermediate appellate court that the state's highest court has deliberately let stand. The second concerns the appropriate standard to be used by a diversity court in determining state law when a state intermediate appellate court, but not the state supreme court, has decided a case squarely on point. Because these important issues of diversity practice are intertwined with the issues of Texas law raised by Paribas, this Court may deem it appropriate to consider and resolve both sets of issues itself.

II. ONCE, AS HERE, A STATE SUPREME COURT HAS EXERCISED ITS DISCRETION TO DENY REVIEW OF THE DECISION OF AN INTERMEDIATE APPELLATE COURT, THAT DECISION MUST BE FOLLOWED BY FEDERAL COURTS SITTING IN DIVERSITY

A. The Texas Supreme Court's Denial Of Review In *Kerr Construction* Did Not Constitute A Finding Of Error

Paribas argues that by denying the application for writ of error in *Kerr Construction* with the notation "writ denied," the Texas Supreme Court indicated that the decision "contained one or more errors of law." Paribas Br. 20. This completely misconceives the significance of the

notation "writ denied." That notation carries with it no suggestion that the decision of the intermediate court of appeals was erroneous. To the contrary, as is explained by the very authors on whom Paribas purports to rely, "writ denied" is precisely "analogous to a 'cert. denied' case in the United States Supreme Court indicating [that] discretionary review in the opinion of the court is not warranted." E. Carlson & R. Garcia, *The New Discretionary Review Powers of the Texas Supreme Court*, 1987 Tex. B.J. 1201, 1204 (Dec. 1987) (hereinafter cited as "Carlson & Garcia"). It is, of course, "well-settled . . . that denial of certiorari imparts no implication or inference concerning the Court's view of the merits." *Hughes Tool Co. v. Trans World Airlines, Inc.*, 409 U.S. 363, 366 n.1 (1973).

Concerning this aspect of Texas appellate practice, it may truly be said that "a page [or so] of history is worth a volume of logic." *New York Trust Co. v. Eisner*, 256 U.S. 345, 349 (1921). Justice Robertson of the Texas Supreme Court laid out the relevant history two years ago in an article that called for and led to a major change in Texas law and practice. *See* T. Robertson & J. Paulsen, *Rethinking the Texas Writ of Error System*, 17 Texas Tech. L. Rev. 1 (1986) (hereinafter cited as "Robertson & Paulsen").

As Justice Robertson described in his article, the Texas Supreme Court had wholly mandatory appellate jurisdiction up until 1917; in that year, although mandatory jurisdiction was retained for certain categories of cases, the court's jurisdictional statute was amended to require the exercise of jurisdiction in most cases only where "it is made to appear that an error of law has been committed by the Court of Civil Appeals, *of such importance to the jurisprudence of the state*, as in the opinion of the Supreme Court requires correction." *Id.* at 12, quoting Act of July 1, 1917, ch. 75, § 1, 1917 Tex. Gen. Laws 140,

140-41 (emphasis in article). The purpose of this amendment was to give "the Supreme Court of Texas . . . discretionary power to grant applications upon consideration of general jurisprudential interests." *Id.* at 13. Both bench and bar expressed considerable opposition to this discretionary review power, however, and "[t]he experiment came to an end in 1927 when the discretionary review language [*i.e.*, the reference to jurisprudential importance] was removed from [the statute]." *Id.* at 16.

For the next 60 years, the Texas Supreme Court struggled to cope with a system of wholly mandatory jurisdiction. During this time, the court evolved three formal notations for denial of review on application for writ of error: "The application may be 'Dismissed' (whether for want of jurisdiction, mootness or by agreement of the parties), it may be 'Refused,' or it may be 'Refused, No Reversible Error.'" Robertson & Paulsen at 26. Whereas "'Writ Refused' . . . mean[s] that 'the judgment of the Court of Civil Appeals is a correct one and . . . the principles of law declared in the opinion are correctly determined,'" *id.* at 19-20, quoting Law of June 14, 1927, ch. 144, § 1, 1927 Tex. Gen. & Spec. Laws 214, "in current practice an 'N.R.E.' can mean virtually anything." *Id.* at 27.[2]

The pervasive ambiguity of the notation "writ refused n.r.e." had two sources. First, even in cases where the opinion of the court of appeals was correct in every respect, the "n.r.e." notation would be used if the application for a writ of error had not met certain technical requirements. Robertson & Paulsen at 30-32. Second,

> even if all formal requirements for refusal are met, failure to "Refuse" the application may not be a negative comment on the lower court decision. As

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[2] Exxon's reply brief in support of the petition for a writ of certiorari mistakenly transposed the meanings of "writ refused" and "writ refused n.r.e." Exxon Reply Br. 5.

> Justice Simpson observed: "It may be that the court, being satisfied as to the correctness of the judgment, did not consider the questions discussed of sufficient novelty or importance to warrant the 'fine-tooth comb' treatment essential to an unqualified approval of an opinion."

Id. at 33 (footnote omitted).

"In summary, the 'N.R.E.' notation could mean that the court of appeals' opinion is very good, since a perfectly faultless opinion may for one reason or another not be marked 'Refused.' " Robertson & Paulsen at 34. On the other hand, the notation also could apply "to decisions riddled with [harmless or] unpreserved error." *Id.* at 37. The meaning of the "n.r.e." notation thus "is often undecipherable in the context of a particular case," *id.* at 59, even though it referred to an action that, because it represented an exercise of mandatory jurisdiction, "is in every sense a decision on the merits." *Id.* at 26. Consequently, Justice Robertson called for the abandonment of mandatory jurisdiction and the confusing system of notation that it had spawned. He argued strongly that the time had come for the adoption of a system of discretionary review. *Id.* at 59-73.

Justice Robertson struck a responsive chord. The Texas legislature acted with alacrity to confer discretionary review powers on the Texas Supreme Court, and it did so by restoring to the jurisdictional statute virtually the same language that it had used for the same purpose in 1917. *See* Carlson & Garcia at 1203. The court promptly made a conforming change in the appellate rules, deleting the "n.r.e." notation and replacing it with the new notation "writ denied." Tex. R. App. P. 133(a).

The new statute, like its predecessor, describes the court's jurisdiction in terms of cases "in which it appears that an error of law has been committed." Act of

June 19, 1987, ch. 1106, § 1, 1987 Tex. Sess. Law Serv. 7649, 7650 (Vernon). Similarly, new Tex. R. App. P. 133(a), like its predecessor, speaks in terms of "cases where the Supreme Court is not satisfied that the opinion of the court of appeals in all respects has correctly declared the law." Paribas seizes upon these archaic formulations to argue that the new notation "writ denied" necessarily means that the lower court's decision was erroneous. It may be conceded that the statute and rule are not felicitously phrased. But it is beyond question that, with minor differences not relevant here, the notation "writ denied" represents a continuation of the former "n.r.e." practice in the context of discretionary rather than mandatory review. Because not even the "n.r.e." notation signified the existence of error, *a fortiori* the notation "writ denied" does not do so. The very article cited by Paribas explains:

> in Texas under the new discretionary review a "writ denied" merely means that for whatever reason, four justices did not vote to "grant" the case. . . . [I]t may very well be that the court of appeals opinion presents no reversible error . . . .

Carlson & Garcia at 1202.

In short, the Texas Supreme Court may "refuse" an application for writ of error, which is equivalent to summary affirmance in this Court; or it may "deny" the application, which is analogous to this Court's denial of certiorari. Like a denial of certiorari, the notation "writ denied," which the Texas Supreme Court employed in denying review in *Kerr Construction*, casts no aspersions whatsoever on the opinion of the lower court. It signifies a purely discretionary denial of review indistinguishable from that employed by the highest courts of all the other 32 states that have intermediate courts of appeals. *See* Robertson & Paulsen at 2 n.5.

B. Denial Of Review Establishes *Kerr Construction* As The Dispositive Statement Of Texas Law For Purposes Of This Diversity Litigation

In *Hicks v. Feiock*, 108 S. Ct. 1423, 1428 (1988), this Court stated that where the highest court of a state has exercised its discretion to deny review of a decision of an intermediate court of appeals, a federal court is "not at liberty to depart from the state appellate court's resolution of these issues of state law." In support, the Court quoted the following passage from *West v. American Tel. & Tel. Co.*, 311 U.S. 223, 237-38 (1940) (emphasis added):

> Where an intermediate appellate state court rests its considered judgment upon the rule of law which it announces, that is a datum for ascertaining state law which is not to be disregarded by a federal court unless it is convinced by other persuasive data that the highest court of the state would decide otherwise. . . . *This is the more so where, as in this case, the highest court has refused to review the lower court's decision* rendered in one phase of the very litigation which is now prosecuted by the same parties before the federal court. . . . Even though it is arguable that the Supreme Court of [the state] will at some later time modify the rule of [this] case, whether that will ever happen remains a matter of conjecture. In the meantime *the state law applicable to these parties and in this case has been authoritatively declared by the highest state court in which a decision could be had.* . . . We think that the law thus announced and applied is the law of the state applicable in the same case and to the same parties in the federal court and that *the federal court is not free to apply a different rule however desirable it may believe it to be, and even though it may think that the state Supreme Court may establish a different rule in some future litigation.*

See also Stoner v. New York Life Ins. Co., 311 U.S. 464, 467 (1940) (diversity courts have a particular obligation to follow the decision of a state intermediate appellate court where that "court has determined the precise question in issue . . . and the highest court of the state has refused review").

To be sure, *Hicks*, *West*, and *Stoner* are different from this case. In each of those cases, the state litigation had involved the same parties who were before the federal court (and *Hicks* itself came before this Court on direct review of the state decision). But this distinction does not point to a different conclusion concerning the deference due to a state intermediate appellate decision that the state's highest court has deliberately let stand. In diversity litigation, such a decision should be accepted as a dispositive and governing pronouncement of state law where, as here, it is not directly contrary to a decision of the state supreme court or that of any other intermediate appellate court within the state. This is so for two important reasons.

First, such a rule of deference serves the ends of both comity and convenience. Federal courts' defeernce to state appellate decisions that have been denied review reflects a suitable recognition of state appellate courts' superior competence in matters of state law. It also frees the federal courts from having to rethink questions of state law in cases essentially identical to those already adjudicated by the state courts.

Second, such a rule of deference would appear to be a necessary corollary of *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938). Although a state supreme court's discretionary denial of review may not express unqualified approval of the lower court's decision, it does dispositively fix the result actually reached in parallel state litigation. The same result also should be reached in federal court: "[t]he nub of the policy that underlies *Erie* . . . is that

for the same transaction the accident of a suit by a nonresident litigant in federal court instead of in a State court a block away should not lead to a substantially different result." *Guaranty Trust Co. v. York*, 326 U.S. 99, 109 (1945).

Deference appears particularly appropriate here. Although as a technical matter denial of review in *Kerr Construction* constituted an expression of neither approval nor disapproval, it is reasonable in the circumstances to infer that the Texas Supreme Court in fact approved of the result in that case. The issuing bank in *Kerr Construction* called the Texas Supreme Court's attention to the contrary decision of the Fifth Circuit in this case. *See* Paribas Br. 10A. In view of this evident conflict, if the court had believed that the Fifth Circuit's decision was correct, or that the decision of the lower court in *Kerr Construction* was questionable, presumably it would have acted on that belief by reversing or granting plenary review. Because the court instead deliberately let stand the result in *Kerr Construction*, Exxon should be granted the benefit of the same legal rules that governed the litigants in that case.

III. *KERR CONSTRUCTION* MUST BE FOLLOWED FOR THE ADDITIONAL REASON THAT THERE IS NO CONVINCING EVIDENCE THAT THE TEXAS SUPREME COURT WOULD REACH A CONTRARY RESULT

Paribas argues that the decision below was correct, and the decision in *Kerr Construction* incorrect, as a matter of Texas law. Paribas Br. 13-19. That argument not only errs in its analysis of Texas legal principles but also misconceives the role of a federal diversity court in applying state law. Even if no application for a writ of error had been filed and denied in *Kerr Construction*, that decision would govern here.

Paribas begins by suggesting that, in the absence of an authoritative decision by the state supreme court, a fed-

eral diversity court is free to decide an issue of state law largely as a matter of first impression. Paribas Br. 13-14. Paribas relies upon two cases, *Commissioner v. Estate of Bosch*, 387 U.S. 456 (1967), and *King v. Order of United Commercial Travelers of America*, 333 U.S. 153 (1948), which explain that a diversity court need not treat an unreviewed decision of a state *trial* court as controlling. But in *Bosch* (as in last Term's decision in *Hicks*) the Court expressly reaffirmed the statement in *West*, 311 U.S. at 237, that the decision of "an intermediate appellate state court . . . is a datum for ascertaining state law which is not to be disregarded by a federal court unless it is convinced by other persuasive data that the highest court of the state would decide otherwise." *See* 387 U.S. at 465.

Neither *Bosch* nor any other more recent decision of this Court disturbs the rule that "[a]n intermediate state court['s determination] in declaring and applying the state law . . . , in the absence of more convincing evidence of what the state law is, should be followed by a federal court in deciding a state question." *Fidelity Union Trust Co. v. Field*, 311 U.S. 169, 177-78 (1940). *See also Lucas v. United States*, 807 F.2d 414, 418 (5th Cir. 1986) ("in the absence of a direct holding by the highest court in a state, we should defer to the holdings of lesser courts unless we are *convinced* by other evidence that the state law is otherwise") (emphasis added). This rule of decision places a heavy burden of persuasion on the party that seeks to avoid application of a ruling by a state intermediate appellate court. Paribas has not carried that burden.

The Fifth Circuit, of course, did not apply the rule of decision articulated in *West* and *Fidelity Union Trust*. Because the court refused to consider *Kerr Construction*, it had no occasion to determine whether other sources of authority constituted "more convincing evidence of what the state law is." *Fidelity Union Trust*, 311 U.S. at 178.

That consideration, in and of itself, renders the court's decision fundamentally unsound as a matter of federal diversity practice. Moreover, if the court had undertaken to make the determination required by such cases as *West* and *Fidelity Union Trust*, it would have been forced to conclude that *Kerr Construction* controls this case.

Atlhough Paribas asserts that "[t]he Fifth Circuit comprehensively evaluated and applied Texas law to resolve the issues presented to it," Paribas Br. 14, that is manifestly not true. Whereas Paribas now cites and discusses a total of *thirteen* Texas decisions, *id.* at 15-19, the Fifth Circuit itself cited only *two*—one at the end of a string cite, J.A. 70 n.7, and the second as an unexplained "cf." cite. J.A. 73 n.18. It is evident from the court's opinion that the panel majority did not decide the case on the basis of an analysis of Texas authorities. If the majority had "comprehensively evaluated" the existing body of Texas law, it would have concluded, even apart from *Kerr Construction*, that, as Judge Garza stated in his dissenting opinion, "the Texas judge sitting on the court below, interpreting the letter of credit under Texas law, was correct." J.A. 76. *Cf. Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 204 (1956) ("[s]ince the federal judge making those findings is from the Vermont bar, we give special weight to his statement of what Vermont law is").

The result in *Kerr Construction* was dictated by well-established Texas rules of contract construction. *See* Exxon Br. 16-19. Paribas argues as if these rules do not apply to letters of credit, which Paribas appears to suggest are subject to different and special rules of construction under Texas law. That suggestion is manifestly incorrect. "Letters of credit are governed by the con-

struction rules of ordinary contracts." *Temple-Eastex Inc. v. Addison Bank*, 672 S.W.2d 793, 798 (Tex. 1984). Letter-of-credit cases do not constitute a separate and hermetically sealed body of Texas jurisprudence, and the *Kerr Construction* court did not err in applying ordinary contract principles to that case.

In any event, the letter-of-credit cases that Paribas cites do not address the question of Texas law presented by this case and decided in *Kerr Construction*. At most, the cases announce principles that govern other types of disputes concerning letters of credit; those principles are fully consistent both with the rules of contract construction applied in *Kerr Construction* and with the actual result in that case.

Paribas relies centrally upon the statement that a beneficiary, such as Exxon, must " 'strictly comply with the terms and conditions of the letter of credit.' " Paribas Br. 16, quoting *Fina Supply, Inc. v. Abilene National Bank*, 726 S.W.2d 537, 542 (Tex. 1987). But that statement, read in context, describes the duty of the beneficiary to present documents that strictly conform to the documentation required by the certification provision of a letter of credit. That duty is important because "the issuer has a *primary* obligation that is dependent *solely* upon presentation of conforming documents and not upon the factual performance or nonperformance by the parties to the underlying transaction." *Republic National Bank v. Northwest National Bank*, 578 S.W.2d 109, 115 (Tex. 1979) (emphasis in original). The duty to present conforming documents is not at issue here. It is undisputed that Exxon presented conforming documents (and thus the question that Paribas seeks to raise concerning its ability to claim reimbursement from Houston Oil, *see* Paribas Br. 17, does not arise).

Nor is this a simple case of a beneficiary failing to make a timely presentation of documents prior to the expiration date. *Cf.* Paribas Br. 16-17. Instead, the ques-

tion of Texas law in this case, as in *Kerr Construction*, is whether a letter of credit will be construed and enforced in a manner that renders the beneficiary's performance impossible and thereby renders the undertaking for which the issuing bank has charged a fee illusory and meaningless. No case cited by Paribas addresses this question. The Texas Supreme Court, however, has given fair warning that a letter of credit will not be construed in the manner for which Paribas argues here. It has instructed on several occasions that a letter of credit should not be read in a manner "that renders its performance impossible or meaningless." *Temple-Eastex*, 672 S.W.2d at 798. *Accord*: *Republic National Bank*, 578 S.W.2d at 115. *See also Breathless Associates v. First Savings & Loan Ass'n*, 654 F. Supp. 832, 836 (N.D. Tex. 1986) ("[t]he Texas Supreme Court indicated in *Westwind* [*Exploration, Inc. v. Homestead Savings Ass'n*, 696 S.W.2d 378, 392 (Tex. 1985),] that constructions of a letter [of credit] that would make performance impossible should be avoided").

Paribas nevertheless argues that courts in other jurisdictions "have uniformly held that the impossibility of compliance with conditions of a letter of credit prior to its expiry date is not grounds for ignoring or changing that date." Paribas Br. 18. The decisions that Paribas cites do not stand for that proposition. In *Liberty National Bank & Trust Co. v. Bank of America National Trust & Savings Ass'n*, 218 F.2d 831 (10th Cir. 1955), for example, the effect of the expiration date was simply to make the letter of credit inapplicable to a shipment that had not been delivered as of that date; the letter remained applicable to a shipment that had been delivered earlier. Similarly, there was no inconsistency or impossibility in *Hyland Hills Metropolitan Park & Recreational District v. McCoy Enterprises, Inc.*, 554 P.2d 709 (Colo. Ct. App. 1976); the letter of credit at issue there required only that the beneficiary submit a

signed statement that a tennis court had not been constructed on or before the expiration date. Indeed, there appears to be no decision in any court, other than the Fifth Circuit's decision here, that enforces an expiration date that literally renders the issuer's undertaking illusory and meaningless.

Paribas' remaining arguments concerning Texas law are insubstantial. The decision in *Kerr Construction* did not constitute a judicial "modification" or "reformation." Paribas Br. 17, 18. It involved the construction of an internally contradictory contract, and the contradiction was resolved by construing the letter of credit as permitting presentation of documents on the last date given in the certification provision for performance of the underlying contract. This construction conformed with the rule that "[i]n Texas, a writing is generally construed most strictly against its author . . . . As a result, the bank's letter of credit is construed most strictly against the bank because it drafted the letter of credit." *Temple-Eastex*, 672 S.W. 2d at 798. *See also, e.g., Willow Bend National Bank v. Commonwealth Mortgage Corp.*, 722 S.W.2d 12, 13 (Tex. App. — Dallas 1986, writ ref'd n.r.e.). Paribas suggests that this rule should not be applied here because its customer Houston Oil had supplied "the essential language used in the letter of credit." Paribas Br. 19 n.14. It may be assumed that the customer normally supplies the terms. This does not, however, excuse the issuing bank from the rule of strict construction stated in *Temple-Eastex*. Moreover, Paribas' suggestion that a bank may be relieved of its entire contractual obligation merely because it deliberately drafted an internally contradictory letter of credit, *see* Paribas Br. 19, must be rejected as grossly inequitable.[3]

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[3] Finally, Paribas argues that *Kerr Construction* should not be followed here because of minor factual differences between the two cases. Paribas Br. 23. Those factual differences, however, are truly insignificant; they have no bearing upon the application of the legal principles that the court in *Kerr Construction* found controlling.

In summary, *Kerr Construction* was correct as a matter of Texas law. A diversity court need not, however, actually determine the correctness of a decision such as *Kerr Construction*. It need determine only that there is no "convincing evidence" that the decision was incorrect. *Fidelity Union Trust*, 311 U.S. at 178. Because Paribas has presented no such convincing evidence, *Kerr Construction* must be followed in this case.

CONCLUSION

The judgment of the court of appeals should be reversed. In the alternative, the judgment should be vacated and the case remanded for reconsideration in light of Texas law, including the decision in *Kerr Construction*, or the question of Texas law should be certified to the Texas Supreme Court.

Respectfully submitted,

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